

Committee on Ways and Means

H.R. 4297, *Tax Relief Extension Reconciliation Act*

Exceptions from Double Taxation under Subpart F

Current Law

Subpart F of the tax code requires U.S. companies to pay immediate tax on earnings from their foreign subsidiaries even if those earnings have not been brought back to the United States. An exception is made for active business income. This “active financing exception” (AFE) is scheduled to expire next year.

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The AFE is extended for two years (through 2008). In addition, cross-border payments of dividends, interest, rents and royalties are also excluded from Subpart F through 2008 if such earnings are attributable to active business earnings.

Benefits of the AFE

- The AFE helps domestic manufacturers that finance sales of large equipment to foreign customers. The AFE allows manufacturers to price these transactions competitively.
- In addition, the AFE keeps the U.S.-based financial services industry on equal footing with its foreign competitors, as no other country imposes immediate taxation on financial services income earned abroad.
- A long-term extension of the AFE is necessary so that U.S.-based companies can engage in long-range, multi-year business planning. Without a long-term extension, domestic manufacturers and financial service firms cannot competitively price long-term products, such as loans and leases.
- The expansion of the Subpart F exception recognizes that cross-border payments of dividends, rents and royalties should appropriately be taxed in the same manner as active income if they are funded with active income that has not been repatriated. This expansion simply follows established rules and allows U.S. companies to effectively respond to market and investment opportunities.